

Internal Revenue Service
Director, Exempt Organizations

Department of the Treasury
P.O. Box 2508 - Room 7008
Cincinnati, OH 45201

Date: JUN 10 2003

Employer Identification Number:
[REDACTED]

Person to Contact - I.D. Number:
[REDACTED]

Contact Telephone Numbers:
[REDACTED]
[REDACTED]

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure 1.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a Trust, or Form 1120 if you are a corporation or an unincorporated association. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice

[REDACTED]

Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that:

A declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely,

W. J. Lerner

Director, Exempt Organizations

Enclosures:

Enclosure I
Form 6018
Publication 892

cc: [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

ENCLOSURE I

Facts

A review of your Articles of Incorporation shows that you were incorporated in [REDACTED]. You are organized exclusively to develop, on a non-profit basis, a housing project for persons of low income at [REDACTED].

You state in your application that your purpose is to combat community deterioration and provide relief of the poor and distressed in [REDACTED] through the development of supportive housing for low-income families, some of which were formerly homeless. You state that, to achieve this objective, you intend to develop and to hold title to a project known as the [REDACTED] ([REDACTED]).

[REDACTED] and [REDACTED] and [REDACTED] section 501(c)(3) organizations, are your sole members and sponsors of the [REDACTED]. These two organizations are also the [REDACTED] and the [REDACTED] of the [REDACTED].

[REDACTED] will consist of [REDACTED] efficient, low-income housing tax credit units, [REDACTED] two-bedroom superintendent's unit, and [REDACTED] storefront commercial unit in a single building. You state that [REDACTED] or [REDACTED] units will be for homeless persons with psychiatric or physical disability, referred from [REDACTED] or from transitional housing operated by local service providers, and [REDACTED] or [REDACTED] units will be for low-income residents of [REDACTED].

The commitment letter from the prospective investor states that the general partner shall make an in-kind contribution of \$ [REDACTED] of the value of the land upon which the [REDACTED] will be built. Section [REDACTED] of the draft partnership agreement provides that the general partner has made or shall make, upon the execution of the partnership agreement, a capital contribution of \$ [REDACTED], consisting of the beneficial and equity interest in the land, in exchange for [REDACTED] of the general partner interest.

You state, in your correspondence to the Service concerning your application, that you have abandoned the above contribution arrangement. You submitted the Amended and Restated Limited Partnership Agreement executed on [REDACTED] (the [REDACTED]) of the [REDACTED] (the [REDACTED])

ENCLOSURE I

[REDACTED], which does not include that \$ [REDACTED] proposed contribution. [REDACTED] shows that the General Partner is [REDACTED] with [REDACTED] interest, and that the Limited Partner is [REDACTED] with [REDACTED] interest. The Partnership Agreement shows that you have no ownership interest in or are not a partner of the Partnership. [REDACTED] is your wholly owned for-profit corporation.

You state in your correspondence that the organizational structure utilizes a for-profit corporation for two primary reasons: First, the for-profit corporation provides another layer of liability protection for you and your sponsors against potential litigation involving the [REDACTED]. Second, the preferred vehicle for tax-credit purposes is a for-profit corporation acting as the General Partner in the Partnership.

Section 2.2 of the Partnership Agreement states that the purpose of the Partnership is (a) to acquire, construct, own, finance, lease, and operate the project property as a qualified, low-income housing project within the meaning of section 42 of the Code; (b) to eventually sell or otherwise dispose of the property in a manner consistent with the Partnership Agreement; and (c) to engage in all other activities incidental or related thereto.

[REDACTED]e, [REDACTED], and the [REDACTED] show that you obtained a loan from the [REDACTED] and acquired the land for \$ [REDACTED]. You then assigned the land and the loan to the Partnership the same day of the execution of the Partnership Agreement through the [REDACTED] and [REDACTED].

[REDACTED] and the [REDACTED] show that you hold legal or record ownership of the property and such ownership shall only be as nominee legal or record titleholder on behalf of the Partnership. You assign and transfer all beneficial and equitable interest in, to, and with respect of the property and the improvements including all rights, title, claims, interest, and obligations of all documents and instruments to the Partnership for \$ [REDACTED].

You state in your correspondence that you fulfill the requirements of the General Partner, because you are its sole owner. You state that, while the two corporations are separate entities, you, as the titleholder, must ensure that the General Partner and the Partnership comply with all the affordable housing provisions set forth in the Deed, the Regulatory Agreements, the Loan Documents, and the Partnership Agreement.

ENCLOSURE I

[REDACTED]

You state in your correspondence that the Partnership Agreement sets forth the powers and duties of the General Partner and the Limited Partner and grants the General Partner authority to make management decisions for the Partnership. You state that you wholly own the General Partner, appoint its board of directors, and, as a result, control the General Partner and its decisions.

You state in your application that the Partnership is responsible for all management and maintenance of the property, while your responsibility is to monitor the [REDACTED] to ensure that it complies with all affordable housing requirements. You state in your correspondence that failure by you and your for-profit subsidiary to abide by the low-income restrictions set forth in the Deed, the Regulatory Agreements, the Loan Documents, and the Partnership Agreement would be deemed a default and grounds for termination of both corporations' interest in the Project. You state that your for-profit subsidiary must abide by the numerous provisions set forth in the above documents, which state that the building must be maintained as affordable housing, and that your for-profit subsidiary cannot derive any revenue from the [REDACTED] above and beyond the disbursements set forth in the Partnership Agreement. You state that same restrictions also apply to the Limited Partner and to the Partnership.

Law

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable purposes.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states that, in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is

not in furtherance of an exempt purpose.

In Moline Properties, Inc. v. Commissioner, 319 U.S. 436, 438 (1943), the court holds that for federal income tax purposes, a parent corporation and its subsidiary are separate taxable entities so long as the purposes for which the subsidiary is incorporated are the equivalent of business activities or the subsidiary subsequently carries on business activities.

In Britt v. United States, 431 F. 2d 227, 234 (5th Cir. 1970), the court emphasizes that where a corporation is organized with the bona fide intention that it will have some real and substantial business function, its existence may not generally be disregarded for tax purposes.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279, 283 (1945) the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, would destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

Discussion

Section 501(c)(3) of the Code sets forth two main tests for qualification for exempt status. An organization must be both organized and operated exclusively for purposes described in section 501(c)(3). You meet the organizational test, because your Articles of Incorporation contain section 501(c)(3) provisions. You must also satisfy the operational test. The key requirement is that an organization be operated exclusively for one or more exempt purposes.

As the above cited Code, Regulations, and Court Cases demonstrate, the conduct of activities for purposes described in section 501(c)(3) of the Code must be the exclusive purpose of an organization before it can be recognized as exempt from tax under section 501(c)(3) of the Code.

You state that you have an oversight responsibility of the Partnership in ensuring compliance with low-income housing standards, and that you fulfill the requirement of the General Partner because you are its sole owner. You are organized for a single housing project. You seek exemption under section 501(c)(3) of the Code based on the activities of the Partnership, that owns a low-income housing project, and its General Partner.

ENCLOSURE I

You are not a partner in the Partnership. A for-profit corporation of which you wholly own is the General Partner in the Partnership.

The central questions are whether the activity of your for-profit subsidiary and the monitoring of the Project can be considered exempt activities for purposes of determining your qualification under section 501(c)(3) of the Code.

For federal income tax purposes, a corporation is a separate taxable entity, a legal being having an existence separate and distinct from that of its owner. The activity of the General Partner cannot be attributed to you because the General Partner is a separate legal corporation.

You have no ownership interest in and have no managing authority over the affair of the Partnership. Furthermore, monitoring a housing project that is owned and operated by for-profit partners is not an exempt activity as described within section 501(c)(3) of the Code. Under these circumstances, you are not in a position to claim that you cause the Partnership to carry out a charitable purpose of section 501(c)(3) of the Code. Since you have no charitable activity of your own, you may not use activities of the General Partner or the Partnership to solely establish your basis of exemption as indicated in Moline Properties and Britt.

You state that the General Partner, the Limited Partner, and the Partnership must abide by the restrictions set forth in the Deed, the Regulatory Agreements, the Loan Documents, and the Partnership Agreement, which state that the building must be maintained as affordable housing and that your for-profit subsidiary cannot derive any revenue from the Project above and beyond the disbursements set forth in the Partnership Agreement. Sponsoring a low-income housing project that meets the requirements under section 42 of the Code and the rent restriction alone does not necessarily satisfy section 501(c)(3) of the Code. Not all low-income housing projects qualify for exemption under section 501(c)(3) of the Code. Section 2.2 of the Partnership Agreement does not explicitly state that charitable purposes take precedence over profit motives. Unlike section 501(c)(3) of the Code, section 42 does not require that charitable purposes be met. As owners of a low-income housing tax credit project, the Partnership and its partners are obligated to meet the requirements under section 42, they, however, are not obligated to operate within the meaning of section 501(c)(3). The for-profit entities that own and operate the Project have economic goals strikingly different from, and

often in conflict with, the charitable goal of providing low-income housing.

As demonstrated in Better Business Bureau, a single function may actually achieve more than one purpose. If one purpose is non-exempt and substantial in nature, it destroys the exemption regardless of the number and importance of exempt purposes. Regardless of the fact that you may cause the Partnership to provide housing to persons regarded as poor and distressed, obtaining a loan to acquire the land, transferring the land and the outstanding loan to the Partnership, holding nominal title to the land on behalf of the Partnership, and serving as an owner of the General Partner are not exempt activities described within section 501(c)(3). This is so, even though you have a close relationship with other section 501(c)(3) organizations.

Conclusion

Under the facts presented, the Service concludes that you are not operated exclusively for charitable purposes because you do not have a charitable activity.

Accordingly, based on all the facts and circumstances, the Service concludes that you do not qualify for recognition of exemption from federal income tax as an organization described in section 501(c)(3) of the Code.

Form 6018
(Rev. Aug. 1983)

Department of the Treasury - Internal Revenue Service
Consent to Proposed Adverse Action
(All references are to the Internal Revenue Code)

Case Number

Date of Latest Determination Letter

Employer Identification Number

Date of Proposed Adverse Action Letter

Name and Address of Organization

I consent to the proposed adverse action relative to the above organization as shown below. I understand that if Section 7428, Declaratory Judgements Relating to Status and Classification of Organizations under Section 501(c)(3), etc. applies, I have the right to protest the proposed adverse action.

NATURE OF ADVERSE ACTION

☒ Denial of exemption under section 501(c)(3) of the Internal Revenue Code of 1986

☐ Revocation of exemption, effective.

☐ Modification of exemption from section 501(c)() to section 501(c)(), effective

☐ Classification as a private foundation described in section 509(a), effective ****

☐ Classification as an private operating foundation described in sections 509(a) and 4942(j)(3), effective for

☐ Classification as an organization described in section 509(a)(), effective

☐ Classification as an organization described in section 170(b)(1)(A)(), effective

If you agree to the adverse action shown above, please sign and return this consent. You should keep a copy for your records.

If you sign this consent before you have exhausted your administrative appeal rights, you may lose your rights to a declaratory judgement under section 7428.

(Signature instructions on Back)

Name of Organization:

Signature and Title

Date

Signature and Title

Date